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FISCAL IMPACT STATEMENT

LS 6714 | **NOTE PREPARED:** Jan 6, 2006
BILL NUMBER: SB 353 | **BILL AMENDED:**

SUBJECT: Alternative Fuel Use and Production.

FIRST AUTHOR: Sen. Weatherwax | **BILL STATUS:** As Introduced
FIRST SPONSOR:

FUNDS AFFECTED: X GENERAL | **IMPACT:** State & Local
X DEDICATED
FEDERAL

Summary of Legislation: The bill requires the Economic Development Corporation to work with: (1) automobile manufacturers to improve awareness and labeling; and (2) companies to include E85 stations in updates of global positioning navigation software.

The bill provides a property tax deduction for organic waste biomass conversion units. It also provides a tax credit for the purchase of electricity generated from an organic waste biomass conversion unit.

The bill increases the maximum amount of credits that may be granted for biodiesel production, biodiesel blending, and ethanol production. It also extends the tax credit for the retail sale of blended biodiesel to 2010, and eliminates the cap on the maximum amount of credits that may be given.

The bill grants a credit for installing or retrofitting a fueling station to dispense B20 blended biodiesel or E85 base fuel. It also specifies that the definition of gasoline includes ethanol-based fuel, including E85 base fuel.

Effective Date: January 1, 2005 (retroactive); January 1, 2006 (retroactive); March 1, 2006 (retroactive).

Explanation of State Expenditures: *Department of State Revenue (DOR):* The Department of State Revenue would incur some administrative expenses relating to the revision of tax forms, instructions, and computer programs to incorporate the new tax credits proposed in this bill. The DOR also is required to collect recapture taxes from taxpayers receiving refueling station investment credits who convert the property to other uses within three years of receiving the credits. The DOR's current level of resources should be sufficient to implement these administrative tasks.

Indiana Economic Development Corporation (IEDC): The bill requires the IEDC to administer new tax credit programs for investment in fueling station property for use in storing or dispensing B20 biodiesel fuel or E85 base fuel. The IEDC's current level of resources should be sufficient to fulfill these administrative tasks. The December 5, 2005, state staffing table indicates that the IEDC had 39 vacant full-time positions, including one regional office position.

Explanation of State Revenues: *Utility Receipts Tax (URT) Credit:* The bill establishes a nonrefundable credit against the URT for taxpayers that purchase electricity for resale at retail from an individual or entity that operates, and generates the electricity from, an "organic waste biomass conversion unit." The revenue loss resulting from this credit is indeterminable. Depending upon the number of conversion units that currently exist and the response of utilities to this credit, the impact could begin as early as FY 2006, if taxpayers adjust their quarterly estimated tax payments.

Biodiesel/Ethanol Tax Credits: The bill makes changes to existing tax credits for production of ethanol, biodiesel, and blended biodiesel, and for retail sales of blended biodiesel. The changes are as follows:

(1) The bill increases the aggregate credit limit from $20 M to $50 M for the ethanol production, biodiesel production, and blended biodiesel production credits. The new aggregate limit would apply to all credits provided after December 31, 2004. <u>The amount of additional credits that may be claimed due to the new credit limit is indeterminable and depends on IEDC certification of companies for the production credits.</u> The IEDC certified $12 M in ethanol production credits in 2005 for four companies, with each company receiving $3 M in credits. No more ethanol production credits may be certified under current statute. <u>With the new credit limit, the IEDC could increase credits to the companies already certified by $2 M each (a total of $8 M in additional credits).</u> The IEDC has not certified any credits for biodiesel or blended biodiesel production.

(2) The bill moves the sunset date for the blended biodiesel retail sales credit from December 31, 2006, to December 31, 2010. The bill also eliminates the $1 M credit limit applicable to all taxpayers and all taxable years. <u>The additional credits that might be claimed due both to extending the time frame of the credit and eliminating the credit limit is indeterminable and depends on IEDC certification of sales credits.</u> In 2005, the IEDC did not certify any credits for the retail sale of blended biodiesel.

Fueling Station Investment Credits: The bill establishes separate nonrefundable Adjusted Gross Income (AGI) Tax credits for qualified investment in depreciable fueling station property in Indiana (other than a building or its structural components) that is used for storage or dispensing into motor vehicles of B20 blended biodiesel or E85 base fuel. The tax credit is effective for purchase, delivery, installation, and refitting expenses incurred after June 30, 2006, and before January 1, 2011. Fueling station property also must be placed in service prior to January 1, 2011, to qualify for the credit. Under the bill, the IEDC administers the credit programs and awards the credits. The bill also provides for a clawback of the tax credit if the creditable fueling station property is converted to another use. <u>While the amount of fueling station investment credits that may be awarded is indeterminable, the bill limits to $5 M the total amount that may be awarded under both credits for all taxpayers and all taxable years.</u>

State Property Tax: The bill establishes an annual AV deduction for "organic waste biomass conversion units." (The definition of an organic waste biomass conversion unit is provided below under the *Background* section on the URT credit.) Property tax deductions exclude property from the property tax base. The state levies a small tax rate for the State Fair and State Forestry Funds that applies to all AV. If property is not a part of the tax base, the state cannot assess this tax on the property. Any decrease in the AV base as a result of deductions reduces the property tax revenue collected for these two funds.

Background - URT Credit: The credit is equal to the additional cost incurred by the taxpayer to purchase the electricity for all rating periods during the taxable year. The bill specifies a formula for determining the additional cost. The bill also requires the Indiana Utility Regulatory Commission (IURC) to disregard the credit amount in determining a taxpayer's utility rates. The taxpayer is entitled to the credit in the taxable year when the electricity is received, and may carry over excess credits for up to three years. The credit is not refundable, and the taxpayer may not carry back excess credits. Revenue from the URT is distributed to the state General Fund. The credit is effective beginning in tax year 2006.

An "organic waste biomass conversion unit" is tangible property that: (1) is not owned by a person primarily engaged in the generation or retail sale of electricity, gas, or thermal energy; (2) the construction of which is reported to the IURC under current statute before construction begins; and (3) is directly used to produce electricity of 80 megawatts capacity or less from agricultural livestock waste nutrients or other agriculture sources, including orchard tree crops, vineyard, grain, legumes, sugar, and other crop byproducts or residues. An organic waste biomass conversion unit includes metering devices, relays, locks and seals, breakers, automatic synchronizers, and other control and protective apparatus designated for safe, efficient, and reliable interconnection to an electric utility's system. However, an organic waste biomass conversion unit does not include tangible property that uses fossil fuel that exceeds the minimum amount of fossil fuel required for any necessary startup and flame stabilization or municipal solid waste.

Biodiesel/Ethanol Tax Credits: Current statute provides credits against a taxpayer's Sales and Use Tax, AGI Tax, Financial Institutions Tax, or Insurance Premiums Tax liability for the production of biodiesel, blended biodiesel, and ethanol, and for the retail sale of blended biodiesel. The tax credits are: (1) $1.00 for each gallon of biodiesel manufactured in Indiana and used to produce blended biodiesel; (2) $0.02 per gallon of blended biodiesel produced in Indiana using biodiesel produced in Indiana; (3) $0.125 per gallon of ethanol produced at an eligible facility in Indiana; and (4) $0.01 per gallon of blended biodiesel sold by Indiana retailers.

Current statute limits the ethanol, biodiesel, and blended biodiesel production credits combined to $20 M for all taxpayers and all taxable years. Within this overall limit, the credits certified by the IEDC must total at least $4 M for each credit. Thus, no new credits for ethanol production can be approved under the current limits, as the IEDC certified $12 M in ethanol production credits in 2005 ($3 M each to four companies). In addition, the taxpayer limit for each credit is $3 M, with provision for the IEDC to increase this limit to $5 M for the ethanol production credit or the biodiesel production credit.

The Alternative Fuels Association (AFA) reports that one ethanol production facility currently operates in Indiana with a capacity of 102 million gallons per year. The AFA also reports that two facilities are currently under construction in Indiana, each with a 40 million gallon annual capacity. The National Biodiesel Board (NBB) reports that there are currently 45 active biodiesel production plants operating in the U.S. and 53 additional production plants proposed, including two in Indiana. The NBB reports that dedicated biodiesel plants in the U.S. have a total capacity of 60 to 80 million gallons per year, and that an additional 200 million gallons of capacity are available from non-dedicated facilities operated by oleochemical producers. The NBB also reports that a total of 59 biodiesel retailers and 41 biodiesel distributors currently operate in Indiana.

Fueling Station Investment Credits: The credit is equal to the lesser of: (1) the qualified investment; (2) $10,000 for all qualified investment by all taxpayers in all taxable years at a single location; or (3) the credit amount awarded by the IEDC. The credit may be claimed only in the taxable year in which the fueling station property is placed in service. E85 fuel contains 85% ethanol and 15% gasoline, while B20 contains 20% biodiesel and 80% petroleum diesel. The bill requires that fueling stations eligible for the investment credit must have common access to a public highway. The fueling stations must dispense the fuel directly into the tank of a motor vehicle propelled by the fuel. The motor vehicle must have at least four wheels and be manufactured primarily for use on public streets, roads, and highways.

The bill requires a credit recipient to pay a recapture tax to the Department of State Revenue if the fueling station property that is the basis for the credit is converted to another use within three years of the taxable year the property was placed in service. The recapture tax is equal to 75% of the credit if the conversion takes place within one year of the tax year the property was placed in service; 50% of the credit if conversion takes place within two years; and 25% if the conversion takes place within three years.

Explanation of Local Expenditures:

Explanation of Local Revenues: *Property Tax Deduction:* The bill establishes an assessed value (AV) deduction for "organic waste biomass conversion units." (The definition of an organic waste biomass conversion unit is provided above in the *Background* section under Explanation of State Revenues.) The annual deduction is equal to the difference between the AV of the taxpayer's property, including the AV of the organic waste biomass conversion unit; minus the AV of the taxpayer's property, excluding the AV of the organic waste biomass conversion unit. The deduction applies to property taxes first due and payable after December 31, 2006. Taxpayers must apply for the deduction in the same manner provided under current statute for the AV deduction for wind power devices.

Additional deductions reduce the AV tax base. This reduction causes a shift of the property tax burden from the taxpayers receiving the deductions to all taxpayers in the form of an increased tax rate. The amount of the deduction is indeterminable. Total local revenues would not be affected, except that the revenue in rate-controlled funds would be reduced.

State Agencies Affected: Department of State Revenue; Indiana Economic Development Corporation; Department of Local Government Finance; State Fair; State Forestry.

Local Agencies Affected: All.

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